*Inquiry into Financial Products and Services in Australia*

Submission to the Joint Committee on Corporations and Financial Services

18 August 2009

## EXECUTIVE SUMMARY

Australians are seeking to build their wealth so that they can live comfortably once they leave paid employment.

To make their money work harder and go further, Australians are increasingly turning to investment options that, if held over the long term and are diversified with risk aligned with their lifestage, can increase savings by more than is possible through traditional banking products such as savings accounts.

There is a social and economic benefit derived from a community seeking to take care of its own lifestage and retirement needs. Responsible investing will assist these needs being met.

We note that the Federal Government's reforms of consumer credit regulation, margin lending and personal properties securities will establish a nationally consistent regulatory framework for the provision of credit in Australia. It will advance public policy outcomes relevant to the Committee's Terms of Reference including enhanced consumer protection measures and responsible lending requirements.

Financial products

ANZ seeks to make its products simple to understand and offers them in a transparent and responsible manner to ensure customers can easily make informed choices.

Margin Lending is a sensible way to invest in the share market when offered responsibly. In our view, this entails ensuring investors are well informed of the nature and risks of the product, investments are diversified, and Loan to Valuation Ratios (LVRs) are suitably prudent. Diversification and prudent LVRs are key aspects of ANZ's approach as these features can reduce the volatility of investments and reduce market and investment risks without sacrificing long-term performance.

Financial services

ANZ's financial planning business (ANZFP) sets high standards for its planners, supports them through ongoing education and training, monitors the quality of advice and addresses any issues that emerge promptly and fairly. Financial services licensees must be satisfied that the products they recommend are suitable for their various client risk profiles, which is achieved through the 'approved product list'. Properly trained planners and products matched to risk profiles are what our clients expect to be delivered by ANZ.

In our view, many of the current concerns about the financial planning industry would be addressed by the further professionalisation of the sector. This could be achieved by the establishment of a professional body that would set entry standards relating to: qualifications; education and ongoing continuing education; register planners; manage claims of misconduct and report findings to ASIC; and oversee a Compensation Fund. ANZ also supports the industry transition to fee-for-service in the provision of holistic financial advice and removing commissions. The obligation of financial planners to put the client's interests first should be legislatively enshrined in order to formally establish that financial advisers owe fiduciary duties to their clients.

It is important to take into account that the further professionalisation of the planning industry and reform of remuneration for planners offering full advice may increasingly put the cost of full advice out of reach of those with small sums to invest or who have simple investment needs. Consideration will also need to be given to how those who are unwilling or unable to afford this advice will be served.

To be able to provide basic financial advice and services to consumers who do not need relatively higher cost financial advice from a financial planner, ANZ has been exploring solutions for these customers through the provision of basic investment products that are straightforward to understand and that are supported by simple advice. Our submission contains more detail about this.

<u>Recent financial collapses</u>

*Opes Prime*

ANZ considers that the existing regulatory framework is comprehensive and contains extensive measures for the protection of both investors and retail users of financial products and service providers. ANZ is not aware of any evidence that the collapse of Opes Prime stemmed from any deficiency in the regulatory framework.

ANZ's own involvement with Opes Prime was limited solely to its capacity as a financier to Opes Prime. In respect of its dealings with Opes Prime, at no time did ANZ have any relationship with Opes Prime's customers. ANZ acknowledges the hardship faced by many clients of Opes Prime as a result of their relationship with the stock broking firm advisory group and the impacts of the global financial crisis and the significant downturn in world debt and equity markets. While ANZ does not consider this to have resulted from its actions, ANZ recognises that at times there were deficiencies in the management of its equity finance business and its relationship with Opes Prime. We have taken appropriate measures to address these issues, which are detailed in this submission.

*Storm Financial*

At no time did ANZ have a formal relationship with Storm. However, ANZ has currently identified around 160 of our customers who may have borrowed from ANZ to invest through Storm Financial. Following the review of the 160 customer files, we have determined that the lending decisions for a small number of customers did not comply with ANZ's credit policies and we are undertaking further review to assess whether others could also be in that group.

We are in the process of contacting those customers who we have identified in our review where our lending policies were not followed correctly. Where it is established that there has been non-compliance with ANZ policies and procedures in lending to these customers we will ensure they are treated appropriately and fairly. Our approach will include assessing financial hardship on a case-by-case basis having regard to their individual circumstances and rectifying financial detriment that resulted directly from any action on ANZ's part.

In addition, we are writing to all other customers we have identified to date, to whom we lent and who were also Storm investors, to invite them to contact ANZ on our toll-free number (1800 280 543) should they wish to discuss their financial circumstances relating to Storm.

We have established a single point of contact in our Hardship Team for affected customers and escalation to ANZ's internal Customer Advocate is available. If the case is not resolved to the customer's satisfaction, we will make available an independent external arbitrator at no cost to the customer.

We have also been working cooperatively with ASIC to provide assistance and information for its review of the collapse of Storm Financial.

We would be pleased to provide any further information about this submission, as required, and can be contacted as follows:

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## 1. ROLE OF BANKS IN PROVIDING FINANCE TO INVESTORS

### (a) Creating a national framework for the regulation of consumer credit

The Federal Government is reforming a number of areas impacting consumer credit that are directly relevant to the Committee's Terms of Reference including:

- Consumer credit regulation: Federal, State and Territory Governments have agreed to transfer regulation of credit to the Federal Government. In addition, the Government is introducing a new licensing regime for all credit providers, intermediaries and debt collectors. From 1 January 2011, credit licensees will need to meet responsible lending obligations which require them to ensure the customer is able to afford to repay without substantial hardship and that the product offered is 'not unsuitable' for the customer's needs and objectives.

  ANZ made a submission to the Australian Treasury Green Paper on Financial Services and Credit Reform and also on the Exposure Draft (both attached). ANZ supports the national regulation of all forms of consumer credit to avoid inconsistency in credit regulation between States and Territories, and to create a single regime that can adapt to changes in the market place more rapidly.

- Margin lending: The Federal Government will regulate margin lending as a financial product under Chapter 7 of the Corporations Act 2001 (*Corporations Legislation Amendment (Financial Services Modernisation) Bill 2009 - Margin Lending*. This will ensure that, from 1 January 2011, anyone offering margin loans or providing advice in relation to margin loans must hold an Australian Financial Services Licence. Margin lenders will also be required to meet responsible lending obligations. This will allow them to provide a margin loan only if they are reasonably sure the borrower is able to afford the loan without suffering substantial hardship. The definition of margin loans in the legislation captures both standard margin loans, as well as more exotic securities lending products such as those used by Opes Prime. This approach is designed to ensure that borrowers and investors are fully informed about the product features of loans. The legislation will also clarify that the party providing the margin loan is responsible for informing the client directly of a margin call unless the client has given instructions to the lender to notify their broker or adviser instead. ANZ's policy is to inform both the client and their broker or adviser directly of a margin call.

  ANZ supports measures that seek to improve disclosure and retail borrowers' understanding of margin loans and made a submission to Treasury (attached) as part of the consultation process. ANZ welcomes the introduction of legislation that would help to reinforce the internal prudential guidelines that banks already generally apply in providing any form of loan. We would also support measures such as an upfront 'key issues' type disclosure which briefly describes the product, outlines the risks and details the costs so as to be of practical assistance to investors.

- Personal Property Securities: The Federal Government will create a national system of personal property securities law that governs how personal property may be used as security for a loan. This will establish a single national personal property securities register that lenders can use to determine whether property (excluding land) provided as security for a loan is subject to any competing claims.

- Comprehensive credit reporting: the Federal Government is considering developing a framework to implement the Australian Law Reform Commission's findings concerning the need for more comprehensive credit reporting arrangements for Australia. ANZ supports comprehensive credit reporting as an important tool in facilitating responsible lending decisions. We understand an exposure draft of the proposed legislation will be released by the end of the year.

**(b) ANZ Responsible lending and responsible products**

ANZ is conscious of its obligations to lend responsibly. ANZ's Customer Charter outlines our commitment to providing convenient, simple and responsible banking services to our customers. It sets out the specific service standards our customers should expect us to meet, including a formal commitment to lending in a responsible and transparent way. While the focus of the responsible lending promises is credit cards, the underlying philosophy is that we will not extend more credit than we assess the customer is able to repay. Each year, our external auditors review our performance against our commitments to our customers and we report the results publicly.

(i) Community understanding of investment fundamentals

Raising understanding of investment principles such as the relationship between risk and return and the importance of diversification in investing is a longer term endeavour and we see this as complementary to the regulatory framework that protects consumers.

As part of our commitment to financial literacy and inclusion, ANZ has initiated and funded ongoing research into levels of adult financial literacy, financial exclusion, and causes of financial difficulty in Australia. This research has led to changes in ANZ's business operations, as well as the development of programs to improve financial literacy levels, especially among the most disadvantaged in our community.

ANZ has undertaken several major research projects on financial literacy. The first, published in 2003, was Australia's first ever national survey of Adult Financial Literacy and provided a benchmark for future research. We published the results of follow-up Adult Financial Literacy surveys in 2005 and again in 2008.

*Findings on investment fundamentals*

Generally, our research has demonstrated that of those who do invest their understanding of investment fundamentals could be improved. Despite a plethora of information freely available, through such sources as www.anz.com or ASIC's FIDO site www.fido.gov.au, our 2008 survey showed a somewhat mixed picture with respect to investing and superannuation.

There were improvements in people's understanding of some investment fundamentals including:

- more people said they would not invest in "*an investment advertised as having a return well above market rates and no risk*", up from 46% in 2002 to 52% in 2008; and
- More people understood that "*short term fluctuations in market value can be expected, even with good investments*", up from 63% to 67% during this period.

However, on a less positive note:

- The proportion of investors who considered diversification of investments to be very important has remained unchanged over the last 6 years - 50% in 2008 compared with 51% in 2002.
- Of those who have used a financial planner, around one in three (35%) did not consider the possibility of a conflict of interest influencing the advice they received.

For our part, ANZ has used and will continue to use the results of our financial literacy research studies to improve our own operations and business practices and to guide product development. ANZ has focussed on making its products simple to understand and offering them in a transparent and responsible manner. Our aim is to ensure customers can easily make informed choices.

(ii) ANZ Personal Loans

While personal loans are available for customers wanting to invest in shares, ANZ does not actively market Personal Loans for that purpose. While ANZ always asks the purpose for which a loan is sought, our focus is on extending a loan the customer can afford. Investment purposes account for only 0.5% of our portfolio.

(iii) ANZ Margin lending

Margin Lending is a sensible way to invest in the share market when offered responsibly. In our view, this entails ensuring investors are well informed of the nature and risks of the product, investments are diversified and Loan to Valuation Ratios (LVRs) are suitably prudent. Diversification and prudent LVRs are key aspects of ANZ's approach as these features can reduce the volatility of investments and reduce market and investment risks without sacrificing long-term performance.

ANZ has over 13,000 borrowers (as at 30 June 2009) that utilise our Margin Loan products. A search of these customers has not revealed any association with either Opes Prime or Storm Financial Ltd. We did not offer any products from either party as approved investments.

*About margin loans*

For the Committee's information, we have outlined ANZ's approach to its margin lending product.

A margin loan allows customers to borrow money to invest in shares or managed funds by using their share portfolio as security for the loan. A margin loan can enable customers to diversify their portfolios by providing a larger pool of money to invest in a wider range of shares or investments.

Diversification and prudent LVRs are key aspects of ANZ's approach as these features can reduce the volatility of investments and reduce market and investment risks without sacrificing long-term performance.

*Margin calls*

When borrowing to invest, it is important to remember that while returns can potentially increase, losses can potentially increase as well. Margin calls are a way of limiting losses.

*How does a margin call occur?*

Falls in the market value of a portfolio can make the Security Value lower than the amount borrowed. To assist in managing the portfolio, ANZ provides a buffer of 5% (explained in the next section) to give customers additional time to take the appropriate actions to return the portfolio to a suitable security position.

If the 5% buffer is exceeded, ANZ will place the account in "margin call." ANZ will then attempt to contact the customer who must either increase their security or repay the loan to the required level.

*What is a buffer and how does it work?*

The buffer exists so that small falls in the market value of a portfolio do not result in a margin call. A margin loan account is 'in the buffer' if the loan balance exceeds the security value by a small amount – less than 5% of the value of the securities.

If a margin loan account is in buffer, further funds may not be borrowed until the account is restored to within normal LVR limits. Whilst there is no need for further action in buffer, it is a reminder to the customer to review the portfolio and to take action to restore it to normal LVR limits and avert a potential margin call.

*Reducing the likelihood of a margin call*

There are several strategies investors can use to reduce the likelihood of a margin call:

- borrow conservatively;
- monitor the portfolio and loan account regularly (real time data and portfolio position is available on My Portfolio, a web based portal offered by ANZ Margin Lending to its customers);
- ensure the portfolio is well diversified to reduce volatility; and
- pay interest monthly rather than allowing it to capitalise on the loan.

*Clearing a margin call*

If the market falls and a margin call occurs on an account, ANZ's policy is to contact both the customer and their adviser.

A margin call must be cleared by close of trade the following business day. There are several ways to do this:

- deposit funds into the loan account or linked cash management account;
- contribute additional ANZ approved securities (shares or managed funds); or

- sell part or all of the existing portfolio to pay down the loan balance so that the Security Value of the portfolio is more than the loan.

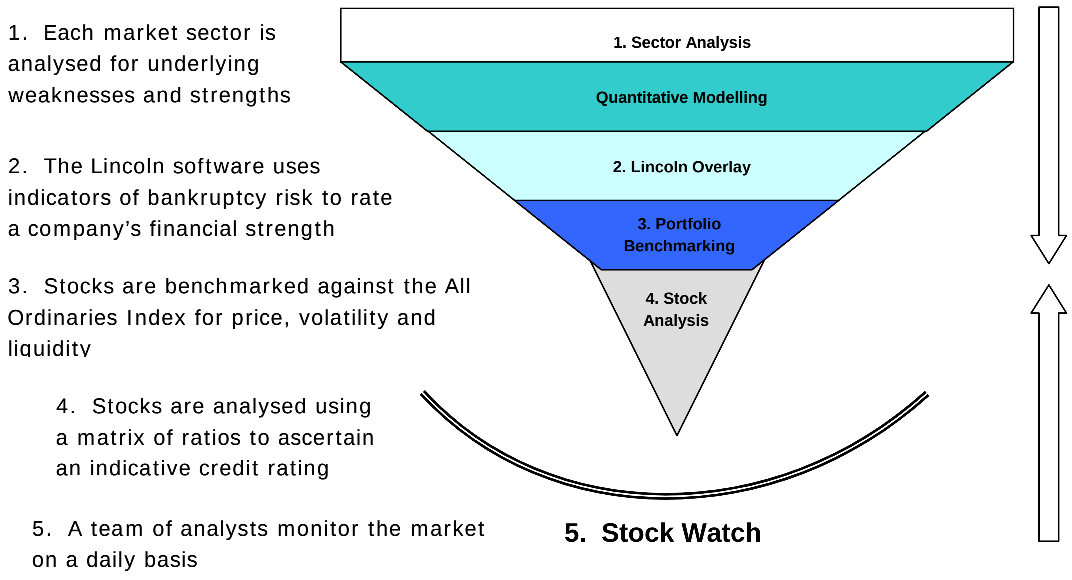
Legal title to the asset resides with the customer until sold. ANZ cannot sell the assets unless a margin call is not met or the customer otherwise consents.

If the customer is not able to clear a margin call by the close of trade the following business day after their account has entered margin call, ANZ will sell enough securities so that the Security Value of the portfolio is more than the loan. This may occur even if we were unable to contact the customer or their adviser. It is important to note that once in margin call, the entire amount of their margin call must be cleared.

<u>ANZ's experience of margin lending</u>

ANZ's approach to risk management is designed to limit investors' exposure to equities or managed funds that are subject to abnormal declines. This approach combines quantitative risk modeling with more targeted analysis of individual stocks and sectors. The following diagram illustrates this approach.

**Diagram 1: ANZ's risk management approach**




The outcome of ANZ's risk approach is the allocation and adjustment of LVRs and the appointment to, or removal from, our Approved Investment List of stocks.

<u>Setting LVRs</u>

Along with understanding and being comfortable with the risks involved with using margin lending products, the principles of diversification and the setting of appropriate LVRs assist customers to manage risk relative to their risk appetite. LVR ratios vary across the industry and ANZ takes a conservative approach with an average LVR of 40%.

The LVR is calculated for individual stocks and managed funds. To ascertain the appropriate LVR, an investment is analysed to determine its financial strength, price volatility and liquidity in the market. These three factors are used to estimate the likelihood of an investment falling in value at greater than the average or benchmark (e.g. the All Ordinaries Index). The lower the likelihood of such a fall, the higher the LVR will be.

For example, a small mining explorer that has relatively few shares on issue, a price that fluctuates dramatically and is financially vulnerable, will have an LVR of 0% to 40% (depending upon the analytical outcome). BHP, on the other hand, has an LVR of 75% which is the maximum for a single stock. Lending against illiquid and small cap stocks is only responsible using modest LVRs or within a diversified portfolio.

ANZ strongly supports and recommends diversification as an investment principle. ANZ margin lending is mostly for diversified portfolio investing as the greatest risk is in single stock or concentrated exposures. A diversified portfolio significantly reduces the probability of margin calls occurring. ANZ offers borrowers a Diversified Margin Loan product that rewards diversification with slightly higher LVRs.

Additional safeguards implemented by ANZ Margin Lending include:

- Stock concentration limits whereby ANZ Margin Lending's total exposure to a single stock does not exceed 5% of total market capitalisation;
- A limit on the maximum credit exposure to a single investor with a non-diversified portfolio;
- Exposure limits to company directors and senior company officers who borrow against their own stock;
- Monitoring total exposures by customer and individual investment;
- No lending directly to managed funds; and
- "Know your Client" analysis to limit the chance of lending to unscrupulous managers or advisers.

<u>Margin Lending and the global financial crisis</u>

ANZ's Margin Lending portfolio was conservatively geared pre-crisis. The loan book was characterised by large numbers of relatively small accounts from ANZ retail channels and small numbers of large accounts, principally sourced from ANZ Private Bank. Gearing levels and utilisation of credit limits were relatively conservative across all segments and few clients contributed sufficient security to utilise their entire credit limit. The market risk-based asset lending approach, outlined above, limited single-stock exposures that posed high risk of "breakthrough" from market to credit risk.

The last 18 months have subjected the Margin Lending portfolio to unprecedented volatility. This resulted in a very difficult environment for margin lending with sustained, broad falls across the market punctuated by sharp single-day volatility and a significant decline in market liquidity. This was exacerbated by the collapse of a number of stocks, including groups of related entities.

The impact on the portfolio included:

- A reduction in total loan portfolio by 33%. Assets mortgaged as security fell by 40%;
- Little net change in active client numbers as the exit of repaying clients has been largely negated by the entry of new clients;
- Credit limit utilisation fell as clients reduced their borrowing but retained their facility limits; and
- Gearing levels were maintained as clients reduced their borrowing in line with the fall in value of their portfolios.

In summary, the fall in the market resulted in a reduction in the average loan size by client as well as a reduction in limit utilisation. Borrowers maintained their limits but, on average, reduced their overall loans.

Clients have maintained similar gearing levels by reducing their loan balances as the value of their security falls. A combination of margin calls and clients' own de-leveraging strategies has reduced exposures in line with reductions in security.

While volatility has caused record numbers of margin calls, cases of negative equity, where customers lose more than their initial investment, are very rare (18 of ANZ's clients are on repayment plans).

## 2. FINANCIAL PLANNING

Australians are seeking to build their wealth so that they can live comfortably once they leave paid employment.

However, it is widely acknowledged that many Australians may not be on track to generate sufficient wealth to achieve a reasonable standard of living in retirement. Smaller superannuation benefits mean more retirees are expected to qualify for a full or part government-funded pension.

To make their money work harder and go further, Australians are increasingly turning to investment options that, if held over the long-term and are diversified with risk aligned with their lifestage, can increase savings by more than is possible through traditional banking products such as savings accounts.

### Current issues

There have clearly been occasions when consumers have been let down, and in some cases significantly so, when they have sought financial advice. Retirement savings have been lost and public confidence in the industry has been undermined. There is accordingly a case for raising standards in the financial planning industry.

Given the ageing of the population and the need, as well as the aspiration, of more Australians to provide for their retirements, the Committee may wish to consider both:

- the need to raise standards within the financial planning industry; and
- the need to do so such that financial services are accessible by a broad section of the community.

Higher standards are likely to have the effect of further raising the cost of compliance and providing advice and may make full service advice less affordable and accessible for those with smaller sums to invest or simple investment needs.

While there is a clear need in many cases for 'high touch' holistic financial advice, many Australians who aspire to build wealth have relatively simple financial needs and may not need, see value in, or be able to afford to pay for advice of this kind.

There is a social and economic benefit derived from a community largely seeking to take care of their own lifestage and retirement needs. Responsible investing will assist these needs to be met. For example, a young person in their 20s starting their first job with $1000 to invest, with a view to saving a deposit to buy a home in their 30s, does not require sophisticated holistic advice, and nor is it economical to seek it. For this category of consumers, ANZ submits that there should be other ways to meet their needs.

### 2.1 Suggested Framework – A two pronged approach

ANZ suggests there is merit in the Committee considering a two pronged approach to the delivery of financial services that includes (i) a full advice option as well as (ii) the provision of cost effective wealth solutions as another option. Such an advice continuum is illustrated in the Diagram on page 14.

### (i) Full Service Advice

Enhance the professionalism of the financial planning industry to improve the quality of investment advice delivered to consumers who require holistic financial advice that takes account of the entirety of their financial circumstances.[1]

In our view many of the current concerns about the financial planning industry would be addressed by increasing the professionalism of the sector. We support tighter regulation of the use of the term ‘financial planner’ to describe those who provide holistic advice. Our view is that, for holistic financial advice, it should be clear that the financial adviser owes a fiduciary duty to the client and accordingly must act only in their interests and must not put themselves in a position where there is conflict with their duty to the client.

Specifically, in order to increase the professionalism of the sector we would support reforms to the sector based on the following principles:

<u>Raising standards</u>

- *Professional body:* A legislatively backed professional body should be established that would be responsible for licensing and registration of planners, setting qualifications, education and training standards and overseeing a disciplinary body that would review conduct by members. This body would be similar to professional bodies that operate in the medical and legal professions and could operate under a similar regulatory framework to that applying to the ASX over ASX participants.

<u>Entry to the profession</u>

- *Registration:* Full Service Advisers should be required to be individually registered by the professional body in order to be permitted to use the name Full Service Adviser. Registration would be contingent on appropriate professional qualifications and continuing professional education.
- *Education Standards*: There should be higher minimum standards than currently required.

<u>Conduct</u>

- *Fiduciary duty to client:* The obligation of Full Service Advisers to put the client’s interests first should be legislatively enshrined.
- *Remuneration:* Full Service Advisers should charge fees for investment advice and should not be permitted to receive commission payments. Clients should be able to choose how to pay the fee for advice, whether out of the product or upfront. We define a fee for advice as a payment made by the client to the planner for their

[1] For the purposes of this paper we use the expression Full Service Advice.

professional advice. We do not think that the basis for calculating fees should be prescribed i.e. it would be acceptable for fees to be calculated as an hourly rate, a percentage of a client's investment or some other measure. What is critical is the client must be able to stop paying the fee should they believe they are not getting value from their adviser. This differentiates it from a commission which is a cost embedded in the product as part of its design, i.e. under current commission structures, if a client leaves an adviser the trailing commission continues to be charged against their account. In these circumstances if the client does not request that the commission be assigned to another adviser, the commission margin is kept by the product manufacturer.

Oversight

- *Misconduct*: the professional body established by legislation should include a disciplinary body to oversee and adjudicate on misconduct by members of the profession and have the power to fine, discipline and deregister individual participants. The findings and any action taken should be reported to ASIC. The combination of individual registration of planners and professional body oversight should help reduce the incidence of 'rogue planners' moving from licensee to licensee.
- *Compensation Fund:* the professional body should establish and administer a compensation fund that is available to meet customer claims, that are established, arising from misconduct of financial planners. Those providing financial advice should hold professional indemnity insurance and the compensation fund should indemnify those who are unable to obtain compensation through their advisers' insurer for negligent advice or fraud.

Accessibility

- *Tax deductibility:* to improve accessibility and affordability of financial advice, it should be tax deductible in the same way that advice provided by accountants and tax advisers is tax deductible.

### (ii) Cost Effective Wealth Solutions

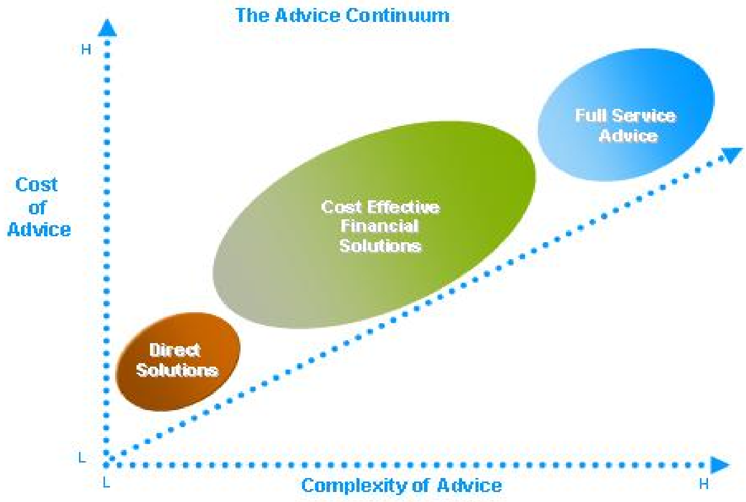
Establish a framework for cost effective wealth solutions for customers with simple needs.

Different frameworks should be discussed under which cost effective wealth solutions may be delivered. What we advocate is that there be a clear delineation between those who provide Full Service Advice and those who offer cost effective 'wealth solutions'. This should ensure that consumers are able to identify the nature of the service being given to them and to understand its implications.

We note at the outset that these possible courses of action are complementary and that they should be implemented concurrently to ensure that the two competing objectives of increased standards and accessibility can be met. If enhancements are made to professionalism on the one hand without addressing issues of affordability on the other, this could have an adverse impact on accessibility.

We also note that there would need to be a period of transition necessary to allow what is discussed here.

**Diagram 1: The advice continuum**




**ANZ's Approach to Financial Planning & Cost Effective Wealth Solutions**

ANZ has made progress in:

- transitioning its Financial Planning business towards a fee for advice model (a transition that is underway but not complete); and
- developing cost effective wealth solutions under the current regime.

We elaborate on this progress in the following section.

**(a) ANZ Financial Planning – the transition to delivering Full Service Advice**

ANZ Financial Planning (ANZFP) is in transition to a full service advice model and the associated remuneration structure. Currently our model is a hybrid of both fees and commissions which will be discussed in greater detail below.

**Overview of ANZ Financial Planning**

ANZ Financial Planning (ANZFP) is a significant financial planning business within ANZ's Wealth business unit, which is part of ANZ's Australia Division. ANZFP has a corporate Head Office with representation across Australia organised into four State-based regions headed by a State manager. The State Manager is responsible for the function of individual Practices in each region that are headed by a Practice Manager.

ANZFP currently has 21 Practice Managers managing 321 Financial Planners across Australia. ANZFP has $9.7 Billion under management for 110,000 clients.[2] Our existing in-force personal insurance book is $97m in premiums across 66,000 clients.

ANZFP Planners provide personal rather than general financial advice. This means that ANZFP Planners must make inquiries about the relevant personal circumstances of the client and give advice that is appropriate to the client given those circumstances.

[2] ANZFP services are offered to all customers of ANZ, other than high net worth customers who are clients of ANZ's Private Bank.

Legislation mandates a range of disclosures that must be given to clients receiving financial advice. These include:

- A Statement of Advice (SOA) that sets out in detail the financial advice given and its basis; and
- A Product Disclosure Statement for any financial products recommended.

**ANZFP's Operating Framework for Financial Planners**

ANZFP's business sets high standards for its Planners, supports them through ongoing education and training, monitors the quality of advice and addresses issues that emerge promptly and fairly. ANZFP has put in place a framework that seeks to ensure that it meets its obligations under law. The core components of ANZFP's framework are:

- Recruitment, Authorisation of Planners and Training
- Educational Standards
- The Formulation and Preparation of Advice
- The Cost of Advice for Clients
- Adviser Remuneration
- Management of ANZFP's Approved Product List
- Monitoring and Supervision of Advisers

**Recruitment, Authorisation of Planners and Training**

All ANZFP Planners are employees of ANZ. As a prerequisite to employment with ANZFP, a Planner must show evidence of: (i) their successful completion of RG 146 training requirements; (ii) the type of advice they are qualified to offer; (iii) the products they advise on; and (iv) the markets in which they operate.

ANZFP Planners are not permitted to provide financial advice until issued with an Authorisation Letter and Practising Certificate. The Authorisation sets out the financial services a Planner is permitted to provide and products the Planner is permitted to advise upon. Planners are authorised to give advice only in relation to the areas in which they have been trained and assessed.

ANZFP may suspend or revoke this authorisation where a Planner does not or is unable to meet their regulatory obligations and their obligations to the client and ANZFP. This may be done immediately and without prior notice to the Planner.

ANZFP provides extensive and ongoing training to its Planners both through internal and external specialist, accredited providers.

*Initial Training*

Before they are authorised by ANZFP to provide financial advice, new Planners must undertake intensive induction training. The induction training is a four-week program designed to introduce and test Planners on the ANZFP advice process, quality requirements and provide specific product accreditation.

Following initial training, an Annual Training Plan is developed for each Planner and these are centrally maintained and monitored by ANZ Advisory Services and ANZFP Risk in a training register.

*Ongoing Training*

Throughout their career with ANZFP, Planners must:

- Complete a minimum of 30 Continuing Professional Development (CPD) points each year. CPD education can include such information as refresher training, best practice education, updates on regulatory changes and compliance policies and is conducted by both internal and external specialist providers;
- Complete a minimum of 120 CPD points every 3 years if they have the Certified Financial Planner (CFP) designation. CFP is the recognised industry body certification;
- Complete any other training requirements identified and agreed in the Planner's Annual Training Plan; and
- Complete any other training mandated by ANZFP.

*Product Training*

Although not a specific legislative requirement, Planners must also undertake Product Knowledge Accreditation programs to ensure they have the knowledge and skills to advise on the products available to clients through ANZFP's business. No Planner may offer products for which they are not accredited. Planner training includes training on asset allocation and diversification.

**Educational Standards**

From 1 October this year ANZFP will require all advisers to exceed current legislated educational standards. We have set a transition period to achieve this goal with a target date of 1 April 2011.

The minimum entry standard for new Planners will be the attainment of an Advanced Diploma in Financial Services with preference given to those who have an FPA approved Degree in Financial Planning. Senior Financial Planners will require either an FPA approved Degree/Masters Degree in Financial Planning or the Certified Financial Planner (CFP) designation. ANZFP is making a significant investment in its Planners' professional development and reimburses all Planners for any approved ongoing education costs.

**The Formulation and Preparation of Advice**

ANZFP utilises COIN Financial Planning Software for financial modelling and plan preparation. Asset allocation benchmarks linked to risk profiles are built into the plan utilising advice from our external research provider, van Eyk Research. We have a centralised paraplanning unit which is responsible for the production of all complex financial plans.

## The Cost of Advice for Clients

*Initial Advice*

In response to public debate about perceived and/or actual conflicts of interest in the financial planning sector, ANZFP now charges a fee for the provision of initial advice as documented in a Statement of Advice.

A minimum fee of $220 (inclusive of GST) is charged for insurance advice and a minimum fee of $550 (inclusive of GST) is charged for investment, superannuation or retirement advice.

*Implementation of Advice*

Should the client wish to progress with implementing their investment advice ANZFP receives revenue via an implementation fee (which is the fee charged for implementing the product solution contained in the advice) and/or product commissions. This implementation fee is based on a percentage of funds invested and capped at 1.1% (inclusive of GST).

*Ongoing Advice*

ANZFP offers its higher net worth customers an ongoing financial advice service (Prime Access) for a yearly fee. Under this scenario any investment product commissions are rebated back to the client. The minimum annual fee for this service is $2,750 p.a. (inclusive of GST).

Ongoing service for non-fee paying customers is paid for by trailing commissions embedded in product solutions and received by ANZFP. These are based on a percentage of funds under advice.

*Ad-hoc Advice*

ANZFP may charge a fee for assistance or services it provides during a financial planning consultation separate to the scenarios outlined above. A minimum fee of $165 (inclusive of GST) may be charged for each 30 minutes (or part thereof) session.

## Adviser Remuneration

ANZFP Planners receive a salary and quarterly bonus based on revenue targets. These targets are determined for each Planner based on a number of criteria. The revenue-based incentives for Planners include revenue from any source including initial advice, implementation and ongoing advice. Incentives are not biased towards a particular product, class of product or class of revenue. Planners are not eligible to receive a quarterly bonus if they have not met ANZFP requirements for compliance and advice quality.

## Management of ANZFP's Approved Product List

There is an expectation with our clients who rely on the ANZ brand that the products ANZFP advise on will perform in line with the risk and return guidelines set out in their Statement of Advice.

Financial services licensees must be satisfied that the products they recommend are suitable for their various client risk profiles. ANZFP discharges this responsibility by establishing an 'Approved Product List' (APL). Subject to tightly controlled exceptions, (e.g. where a customer seeking ANZFP services brings with them an existing investment portfolio) ANZFP Planners may only make recommendations to clients in relation to products on the APL. Our APL has historically taken a conservative approach to investment risk consistent with our reputation as a major Australian financial services institution.

ANZFP has in place a product selection and review Committee to ensure that there is a robust decision-making process for the inclusion and retention of products on its APL. The Committee comprises senior members of the ANZFP management team and a senior representative from Risk.

**Monitoring and Supervision of Planners**

ANZFP's monitoring and supervision framework exists within an ANZ company-wide compliance and risk management framework.

This requires the identification of the primary regulatory compliance obligations impacting ANZFP and the regular preparation and execution of a Compliance Plan to:

- identify compliance risks;
- identify controls in place to mitigate those risks;
- put in place a testing programme to ensure those controls are effective; and
- put in place treatment plans to deal with any compliance risks that may not have sufficient, or sufficiently effective controls.

To do this ANZFP adopts the following measures:

*Planner Audit/Review Process*

ANZFP has a Quality Assurance Review process in place to regularly review Planners and samples of their customer files. This function is undertaken by Quality Managers (QMs) located in all States who report to ANZ Risk, rather than to the ANZFP business.

The annual Quality Assurance Review examines a Planner's advice to clients and the link between the client's individual situation and the quality of the strategies presented; their compliance and strategy knowledge and back office administrative processes.

Quality Assurance reviews use a scorecard to assess those factors that contribute to ensuring the key legislative requirements are met.

*Incident/Breach Management & Reporting*

ANZ has in place an incident reporting and management framework to ensure that it is able to meet its legal incident reporting obligations and to enhance its ability to identify and address systemic issues. This framework is supported by a bank-wide incident recording, escalation and monitoring database that enables us to record, manage and report on incidents internally as well as to regulators when needed.

ANZFP supports this framework and ensures that all of its staff have a clear understanding of their responsibilities for identifying and reporting incidents by ensuring that all Planners and their managers are informed about their obligations to identify and escalate incidents.

*Using the quality review information*

Information obtained from QM reviews of financial plans and Planners and incident reports are used by ANZ Risk and ANZFP management to identify and address any issues and continuously improve.

*Consequences for a Planner*

Consequences for a Planner may include remedial training, loss of bonus, pre-vetting and post-vetting of future client files, additional targeted audits, revocation of Practicing Certificate or dismissal.

A Planner who fails their audit is not entitled to receive a bonus for the quarter in which that audit occurs. If the failure is less severe the Planner is entitled to earn 50% of the bonus provided they undertake and successfully complete the remediation actions set for them within specified timeframes.

Serious adverse findings or repeated audit failure may result in formal first and final warning letters or termination of employment.

**Transition period required for a complete shift to a fee for advice model**

At present the transition of ANZFP towards a pure fee for advice model for new customers is underway but not complete. This transition should be possible by 2012, provided that there is a clear mechanism permitted under any new regime for providing cost effective wealth solutions as described in our submission.

**(b) <u>Cost effective wealth solutions developed by ANZ in the current regulatory environment</u>**

ANZ understands from its customers that many are inhibited from investing for several reasons:

- *Fear* of making a mistake
- *Effort* required to get into investing in terms of locating a Planner, conducting research, finding a broker
- *Time* it takes to maintain and manage an investment portfolio and set it up
- *Knowledge* required and time and effort required to build understanding
- *Cost* of financial advice, transaction costs and fees for broker services etc
- *Risk* of losing their investment, especially if based on a lack of knowledge.

Currently, for those unwilling or unable to pay for full service financial advice, there are two options:

(i) invest in simple investment products that are easy to understand and do not require high levels of training for those suggesting them; or

(ii) obtain advice but pay for it through commissions or other forms of product revenue spread across the life of the product.

This information has been used to help ANZ design some new products that assist consumers who want to diversify their risk and invest conservatively, especially those with simple investment needs or with small sums to invest and who find the cost of full advice uneconomical for their needs.

**ANZ Lite advice pilot**

ANZ is piloting a 'simple advice' model. Called '*My Advice',* the model provides one-off advice via a phone call rather than holistic and ongoing advice. It is designed to provide retail consumers with an appropriate recommendation to either assist them to get started on the wealth accumulation journey or to take steps to protect their family assets against unforeseen circumstances.

To access this advice, a customer calls a 1800 number to speak with a qualified financial planner based at ANZ's Australian Call Centre. These advisers are qualified to provide recommendations on a select range of ANZ savings and investment products that may be suitable to a customer's needs and objectives. The advisers are remunerated by base salary only. Following a conversation about their current situation and future aspirations customers are provided with a Statement of Advice in plain English delivered by email or post.

The investments this service can advise on are limited to selected ANZ bank and investment products, such as the Online Investment Account and Term Deposits. This product offering will be expanded, over time, to include insurance and other investment products appropriate to this segment of the market that requires only limited advice.

No complex advice is provided and customers are advised of this during the consultation. Customers seeking full financial advice are directed to ANZFP.

*My Advice* can help customers to:

- Get started with investing from $1000;
- Find an appropriate savings or investment product; and/or
- Better understand the risk and return associated with their investments.

ANZ believes this option could efficiently provide advice to those with smaller amounts to invest who do not need or want to pay for comprehensive financial advice. For the pilot, some clients are charged a one-off fee-for-service of $100 for the *My Advice* service. The early customer feedback concerning the fee is mixed as those with small sums to invest may still find this initial fee too expensive. In any event, the costs of providing this advice model are still higher than the fee-for-service charged and, as long as product fees are clearly and simply disclosed we see a continuing role for some cost recovery through product fees.

**Online Investment Account**

The latest Australian Share Ownership study (ASX 2009) shows that 6.7 million people, or 41 per cent of adults, participate in the share market. Of these, some 36% are direct investors in shares. While Australians have some of the highest rates of share ownership in the world, as stated previously, our research tells us that many do not invest because of lack of knowledge, fear of investing, not having enough time to devote to managing a share portfolio and the costs and complexity of using brokers.

In response to this research, ANZ has introduced the ANZ Online Investment Account that offers retail banking customers the combination of convenience, simplicity, low fees and diversification. This is a first-of-its-kind share investment product which looks and feels like an online savings account, but is an investment in a fund that tracks the S&P/ASX 200 Index. This means the investment increases or decreases in value, excluding the effects of fees and charges, depending on the daily fluctuations of the index on the ASX.

Customers can monitor their investment performance or increase/decrease funds invested at any time using ANZ Internet Banking and their account details can be viewed online in a simple account statement. ANZ discloses the investment risks prominently, in plain English, including that the account is linked to the performance of the Australian share market which generally has a higher risk than fixed interest investments, term deposits, and traditional savings accounts.

ANZ's Online Investment Account product is in response to customers who may be investing for the first time in the share market and want to do so without the costs and inconvenience involved in using brokers and having to follow individual stocks. It also suits those customers who do not want to spend time and effort managing a share portfolio, including choosing specific stocks and tracking various investments, but who want the higher, longer-term returns that can be derived from diversified share investing.

The ANZ Online Investment Account has relatively low transaction and management costs. Compared to traditional managed funds, the product charges a low management fee (1% pa). First time investors can contribute small amounts on a regular basis – the product allows customers to contribute from as little as $100, for which they will be charged transaction costs of $0.25. When compared to online brokers – this is a considerable cost saving per transaction for a diversified investment.

## 3. SECURITIES LENDING AND OPES PRIME

ANZ considers that the existing regulatory framework is comprehensive and contains extensive measures for the protection of retail users of financial products and service providers.

In particular, the framework provides a sound base for protecting retail clients from loss that could be suffered as a result of purchasing and dealing with financial products through the requirements that financial service providers:

- hold an Australian financial services licence;
- provide a Financial Services Guide, Statement of Advice and Product Disclosure Statement (as appropriate) when providing financial advice or dealing in a financial product; and
- have a reasonable basis for advice provided to a retail client, having regard to the client's personal circumstances (after having made reasonable inquiries regarding those circumstances).

ANZ is not aware of any evidence that the recent corporate collapses, such as Opes Prime, stemmed from any deficiency in the regulatory framework.

Nevertheless, particularly with respect to margin lending facilities, ANZ considers that the existing regulatory regime would be bolstered by the introduction of statutory responsible lending obligations proposed in the *Corporations Legislation Amendment (Financial Services Modernisation) Bill*.

ANZ acknowledges the hardship faced by many clients of Opes Prime as a result of their relationship with the stock broking firm advisory group and the impacts of the global financial crisis and the significant downturn in world debt and equity markets. While ANZ does not consider this to have resulted from its actions, ANZ recognises that at times there were deficiencies in the management of its equity finance business and its relationship with Opes Prime and has since taken appropriate measures to address these issues.

### Securities lending and equity finance

Until its collapse in early 2008, Opes Prime provided securities lending (including equity finance) facilities. In general terms, securities lending refers to the transfer of securities from one party to another in return for cash or other securities ("collateral"). The party who receives the securities is generally obliged to return them (or equivalent securities) either on demand or at the end of an agreed term, subject to repayment of the collateral.

Equity finance is a particular subset of securities lending in which the value of the cash collateral advanced to the party providing the securities ("customer") is generally less than the value of the securities received by the party providing the cash collateral ("financier").

The principal distinction (from a legal perspective) between margin lending and equity finance is that with the latter the customer transfers all legal and beneficial interest in the securities to the financier.

A good description of securities lending and the commercial context in which it occurs is contained in the judgment of Justice Ray Finkelstein in *Beconwood Securities Pty Ltd v Australia ad New Zealand Banking Group Limited* [2008] FCA 594. A copy of the judgment is attached.

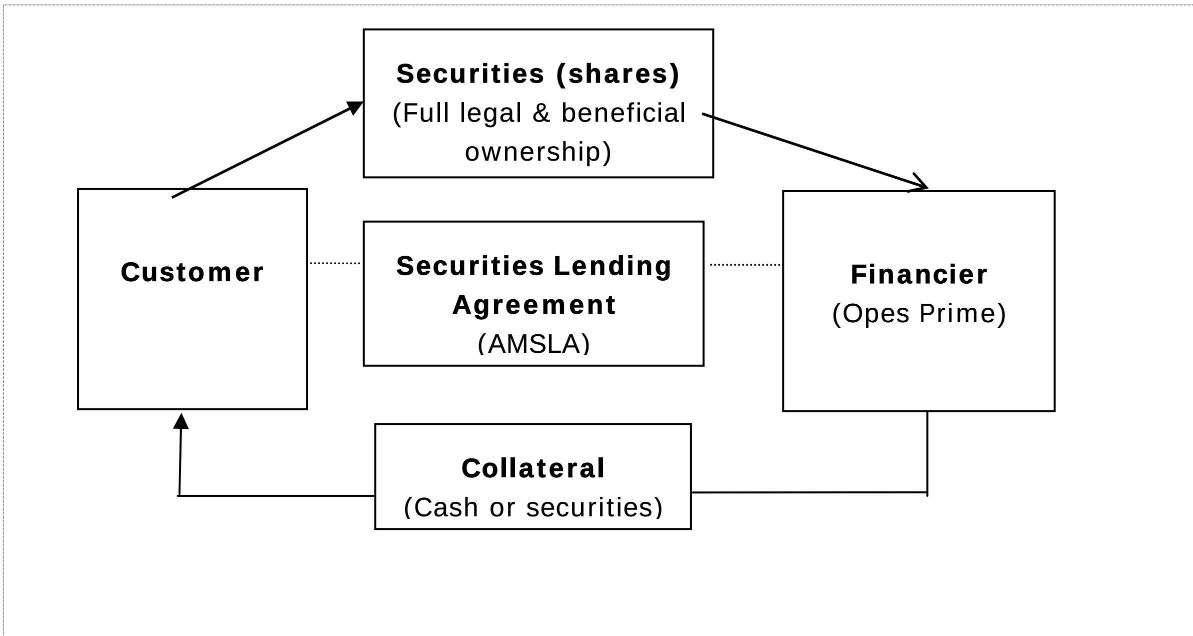
**Opes Prime's business model**

The equity finance transactions between Opes Prime and its customers were made under various securities lending and borrowing agreements based on an Australian Master Securities Lending Agreement (AMSLA). Those agreements provided the contractual basis upon which Opes Prime's customers transferred the legal and beneficial ownership of their securities to Opes Prime in exchange for cash collateral advanced to them by Opes Prime.

The amount of cash collateral provided by a financier is determined by a loan-to-valuation ratio (LVR), which generally reflects the financier's assessment of the quality of the securities being provided by the customer.

On a relatively low quality security, where the financier applied an LVR of, for example, 30 per cent, the financier would then provide cash to the customer equal to 30 per cent of the market value of the security. Where that position deteriorated, such as where the value of the securities fell, the financier could then make a 'margin call,' and the customer would be required to either transfer some additional securities or make payments to the financier in order to maintain the 30 per cent LVR.

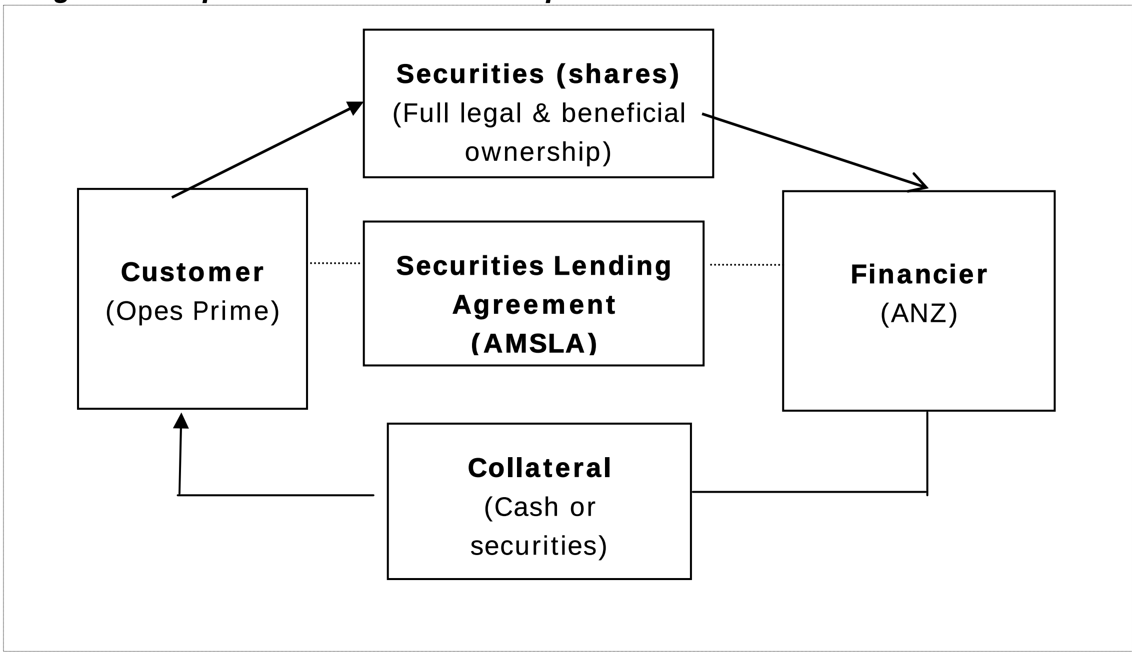
***Diagram 1: Opes Prime's relationship with investors***




In order to raise its own finance, Opes Prime itself entered into AMSLAs with a number of financiers including ANZ, Merrill Lynch and Dresdner Kleinwort. ANZ entered into two AMSLAs with Opes Prime companies, which ran for the duration of ANZ's relationship with Opes Prime.

Under those AMSLAs, Opes Prime would transfer securities to ANZ and in return ANZ would transfer to Opes Prime cash or other securities. ANZ would then return equivalent securities to Opes Prime upon repayment by Opes Prime of the cash or securities. The funds or securities available at any given time to Opes Prime, under the AMSLAs between it and ANZ, were based on an LVR model calculated on a daily basis.

***Diagram 2: Opes Prime's relationship with ANZ***




**ANZ's role as financier to Opes Prime**

ANZ's relationship with Opes Prime was limited solely to its role as financier, primarily through ANZ's securities lending and equity finance business. ANZ also provided some general banking facilities, including small working capital accounts, bank accounts and bank guarantees.

In respect of its dealings with Opes Prime, ANZ did not have any direct relationship with Opes Prime customers. ANZ was not party to the contracts between Opes Prime and its customers and, where securities were transferred to ANZ, ANZ was not provided with documents evidencing the identity of the person from whom Opes Prime obtained the relevant securities.

ANZ's knowledge of Opes Prime's customer base was necessarily limited given that ANZ did not have a direct relationship with Opes Prime's customers. Given that Opes Prime held legal and beneficial ownership of the securities, Opes Prime was not obliged to inform ANZ of the identity of the person from whom they had obtained the securities that it transferred to ANZ.

Since the collapse of Opes Prime, ANZ has come to understand that Opes Prime's customer base was diverse and included a wide range of customers. However, throughout ANZ's dealings with Opes Prime, Opes Prime consistently described its clients as high net worth individuals and sophisticated investors, as well as several stockbroking firms and fund managers.

ANZ also did not possess detailed knowledge of the way in which Opes Prime marketed its products, although Opes Prime stressed to ANZ that it did not provide financial advice, which was consistent with ANZ's then understanding of the sophisticated nature of Opes Prime's customer base.

**Opes Prime's collapse**

In early 2008, ANZ decided to tighten the management of the Opes Prime account by implementing a revised LVR model. Had it been immediately applied, the effect of the new LVR model would have been to place Opes Prime into a significant margin call.

Consequently, ANZ agreed that Opes Prime should set a timetable for an orderly migration to the new LVR model, with each milestone gradually reducing Opes Prime's potential margin call to ANZ. Opes Prime set the migration timetable (which extended over approximately two months) in accordance with agreed milestones. The first milestone was to be achieved by 12 March 2008.

Shortly before this date, ANZ was informed that Opes Prime could not in fact achieve the milestone. Consequently, on 13 March 2008, ANZ met with Opes Prime and explained that it sought increased comfort (broadly in the form of security and amendment to certain terms of the AMSLAs between ANZ and Opes Prime), pending a foreshadowed refinance of Opes Prime's facilities by Merrill Lynch. The basis for an agreement was reached, subject to Opes Prime Board approval.

ANZ next met with Opes Prime on 19 March 2008. ANZ understood that the purpose of the meeting was to discuss the issues raised on 13 March 2008. Instead, ANZ was unexpectedly informed by Opes Prime's directors that two serious issues had been uncovered:

- irregularities had been uncovered in respect of the account of one of Opes Prime's customers. ANZ was told that it appeared that Opes Prime's records had been manipulated to make it seem that the customer was within margin, when in fact this was not the case; and
- Opes Prime faced a request for redelivery by a customer of certain securities, valued at approximately $95 million. ANZ was told that the request required redelivery almost immediately. It was explained by the Opes Prime directors that the securities in question were lodged with ANZ and that Opes Prime did not have the funds to pay for the redelivery of those shares from ANZ.

ANZ was informed that without immediate assistance, the directors of Opes Prime would be required to appoint a voluntary administrator.

Given the urgency, ANZ prepared a plan to support Opes Prime. This plan ultimately included a loan of $95m to pay for the redelivery of the securities in question and a seven day 'stand-still' period in respect of margin calls. In return, ANZ sought the comfort it had discussed with Opes Prime on 13 March 2008, including the appointment of Deloitte as an investigative accountant to work with Ferrier Hodgson (Opes Prime's financial advisor) to assess the financial affairs and practices of Opes Prime.

ANZ also confirmed that - dependent on the outcome of the review by Deloitte and Ferrier Hodgson - a longer term work-out would likely be required over the following 6 to 12 months and that ANZ's preferred position was to reach a successful outcome for all parties. Opes Prime agreed to these terms and the documentation was executed on 20 March 2008.

Following 20 March 2008, Deloitte and Ferrier Hodgson commenced their investigative work. It soon became apparent that there were further issues and irregularities in Opes Prime's business.

On 27 March 2008 the directors of Opes Prime appointed Ferrier Hodgson to act as voluntary administrators. Later that day, given the appointment by Opes Prime of the voluntary administrators, ANZ appointed Deloitte as receivers and managers pursuant to a registered charge.

### Impact on Opes Prime customers

While customers of Opes Prime are understood to have signed agreements providing for the transfer of ownership of securities, when a broker such as Opes Prime becomes insolvent, ANZ is seen to be, and in fact is, holding the securities that Opes Prime's customers may have expected would be returned to them. In realising these securities to protect its position, ANZ is regarded by some (including customers of Opes Prime) as acting in its own interests and at the expense of the customers of Opes Prime.

Some of Opes Prime's customers assert that they regarded their arrangements with Opes Prime as some form of margin lending. Some claim that they did not understand that theirs was a full transfer of legal and beneficial title in securities to Opes Prime, and that Opes Prime was then free to deal with these securities without restriction, including transferring them to ANZ.

On 2 May 2008, Justice Ray Finkelstein ruled in a test case in the Federal Court that Beconwood Securities, a customer of Opes Prime, did not have a legal claim to recover its shares under the AMSLA used by Opes Prime. His Honour upheld the effect of the Opes Prime securities lending agreement, finding that under the AMSLA:

- Full title to the shares passed; and
- The Opes Prime customer did not retain an equitable (beneficial) interest.

The fact Opes Prime sourced the securities from its clients was a key distinction between Opes Prime and other parties with whom ANZ entered into similar arrangements. The particular consequences to ANZ of this distinction were demonstrated following the appointment of administrators to Opes Prime. These included reputational consequences, which for ANZ arose primarily as a result of the position in which Opes Prime's customers found themselves. Upon the appointment of administrators to Opes Prime, its customers lost the ability to recall securities that they had transferred to Opes Prime, and instead became unsecured creditors for any 'netted' amounts owed to them under their Equity Finance arrangements with Opes Prime.

**ANZ's response to the Opes Prime collapse**

On 14 April 2008, ANZ's CEO announced a review of ANZ's involvement in Securities Lending and its dealings with Opes Prime. The key conclusions of the Review and remedial actions were announced publicly on 22 August 2008 in a report (attached) which can also be downloaded from www.anz.com.

The Review Committee found that at times there were deficiencies in the management of ANZ's Equity Finance business.

A comprehensive 13 point remediation plan has been developed to address the management control and accountability issues identified in the Review, including the departure of eight managers and executives from ANZ.

Implementing the remediation plan

In implementing its remediation plan, ANZ has reinforced four main values that it perceives as integral to conducting its business:

- encouraging individual accountability;
- improving risk culture;
- enhancing the importance of ethics in decisions and actions; and
- acting consistently with strategy.

To ensure that it acts in accordance with these values, ANZ has commenced implementation of the following measures:

- a complete and orderly withdrawal from all equity finance business and rationalisation of its standard securities lending businesses, so as to limit it to several key multinational institutional relationships;
- improving existing, and implementing new, control frameworks and processes, including:
  - (i) improved Wholesale Credit Risk Policy;
  - (ii) improved product approval processes;
  - (iii) a new Reputation Risk Framework;
  - (iv) a new Performance Management Framework;
  - (v) improved controls around credit limits and customer exposure reporting; and
  - (vi) entering into an enforceable undertaking with ASIC, in connection with its custody and securities processing business, ANZ Custodian Services.

Progress on the 13 point remediation plan has been closely monitored by the Australian Prudential Regulation Authority (APRA), which has identified that ANZ has made good progress in addressing the various issues raised. Of those 13 items, APRA considers that six are closed, one is partially closed and a further five items are currently being reviewed by APRA for closure. The remaining item is currently undergoing review at ANZ before completion and submission to APRA.

In accordance with the enforceable undertaking between ANZ and ASIC, a remediation plan undertaken in ANZ Custodian Services will be reviewed by an appointed independent expert.

In order to ensure that this process is implemented fully, ANZ has worked with its regulators to implement the remediation items and has kept its regulators informed of developments.

Finally, ANZ has reached agreement with the liquidators of Opes Prime for the implementation of a scheme of arrangement between ANZ, Merrill Lynch and Opes Prime and various other related parties and creditors. Agreement was reached following multi-party talks, which were mediated by a former Justice of the Court of Appeal, the Honourable Alex Chernov AO QC. The scheme of arrangement was approved, first by the creditors of Opes Prime, and finally by Justice Ray Finkelstein on 4 August 2009. The scheme will provide Opes Prime's creditors with a significant return on the amounts owed to them by Opes Prime, as a result of ANZ and Merrill Lynch contributing to a settlement figure in excess of $250 million.

**Observations on the existing regulatory regime**

ANZ is not aware of any evidence that the collapse of Opes Prime stemmed from any deficiency in the regulatory framework. To ANZ's knowledge, the directors of Opes Prime were highly experienced in the business of securities lending and equity finance. Each of the directors had worked for many years in the industry.

For its part, although ANZ did not have any direct dealings with the customers of Opes Prime, ANZ recognises that at times there were deficiencies in the management of its equity finance business.

## 4. STORM FINANCIAL

Following a two month review, ANZ has currently identified around 160 of our customers who may have borrowed from ANZ to invest through Storm Financial. We have also been working cooperatively with ASIC to provide assistance and information for its review of the collapse of Storm Financial.

### Review Methodology

Our review team analysed the lending files of the identified customers to assess the quality of the credit decisions and whether they accorded with ANZ's credit policies at the time. We are keeping ASIC apprised of the review process and its findings.

### Key Findings

(i) Customers

The review found that the lending was predominantly by way of home loans secured against property. There were also a small number of personal loans and business loans, which we are reviewing to determine whether they were used for Storm investments. ANZ did not provide margin loans to these customers. Of these loans we have determined that, in some cases, the lending decisions did not comply with ANZ's credit policies.

Following the review of the 160 customer files, we have determined that the lending decisions for a small number of customers did not comply with ANZ's credit policies and we are undertaking further review to assess whether others could also be in that group.

(ii) ANZ's relationship with Storm

The review also identified that these were isolated cases and not part of a formal relationship with Storm Financial. At no time did ANZ have a formal relationship with Storm.

ANZ was approached by Storm in November 2007 seeking a formal referral arrangement. ANZ declined on the basis that the Storm 'business model' was not compatible with ANZ's approach to lending. For example, Storm's preferred approach was that Storm representatives would:

- explain the bank's lending documentation to customers;
- provide the bank with instructions regarding a customer's account maintenance (i.e. renewals);
- would arrange for the customer's 100 point identification check to be completed; and;
- expect the bank to provide a quote for a customer's lending requirements prior to a full application having been submitted.

On the basis that these requirements were unacceptable to ANZ, it was agreed that ANZ could not work with Storm.

## Remedial and accountability actions

We are in the process of contacting those customers who we have identified in our review where our lending policies were not followed correctly.

1. Fair and appropriate treatment

Where it is established that there has been non-compliance with ANZ policies and procedures in lending to these customers we will call these customers and ensure they are treated appropriately and fairly. Our approach will include assessing financial hardship on a case-by-case basis having regard to their individual circumstances and rectifying financial detriment that directly resulted from any action on ANZ's part. This resolution could include, for example, reassessing the amount ANZ would have lent if policies had been adhered to; waiving interest or restructuring the loan to be interest free or reducing the loan amount.

In addition, we are writing to all other customers we have identified to date, to whom we lent and who were also Storm investors, to invite them to contact ANZ on our toll-free number (1800 280 543) should they wish to discuss their financial circumstances relating to Storm. We have a team dedicated and trained to be able to make arrangements quickly and efficiently over the phone wherever possible and where the customer agrees.

2. Dedicated Storm Hardship Team

We have established a single point of contact in our Hardship Team for affected customers to ensure their contact with ANZ is managed by someone familiar with the detail of the cases involved and can provide appropriate information. Escalation to ANZ's internal Customer Advocate is available. The Customer Advocate operates at arm's length to ANZ's business and reports to the Australian CEO. If the case is not resolved to the customer's satisfaction, we will make available an independent external arbitrator at no cost to the customer.

3. Hardship Commitments and options

Where Storm customers are in hardship we have a range of non-traditional repayment options available including:

- repayment deferral with interest waived for the period of the deferral; and
- in special circumstances an interest free loan or reduced loan amount.

We are aware of the hardship experienced by some Storm customers and we have given an assurance that ANZ will seek to work with Storm customers to find solutions to keep them in their homes.